

**UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
Roanoke Division**

IN RE:

**CLYDE T. SHAW
DORIS LEDERER,**

Case No. 01-05217

Debtors

IN RE:

AKEMI TAKAYAMA WIENCKO,

Case No. 01-05219

Debtor

DECISION AND ORDER

At Roanoke in said District this 8th day of June, 2005:

The debtors in the above-captioned cases filed a request for evidentiary hearing on their amended objection to the claim of David Ehrlich (herein Ehrlich) and have noticed the request for hearing on June 15, 2005, at 2:00 p.m. in the United States Bankruptcy Court for the Western District of Virginia, Roanoke Division. Ehrlich, by counsel, filed a response objecting to the notice of hearing and request for evidentiary hearing. Ehrlich argues that there is no basis for the hearing on June 15, 2005, and requests denial of the request for evidentiary hearing on his claim.

The debtors have pending before the court a second amended objection to Ehrlich's claim.¹ The basis for the request for evidentiary hearing is that this court needs to take

¹ See, Exhibit G to docket entry 165.

additional evidence as it relates to the Pennsylvania state court judgment which forms the basis for Ehrlich's claim in order to determine whether Ehrlich's claim falls into any of the subparagraphs of 11 U.S.C. § 502(b) of the Bankruptcy Code which would result in either the disallowance or the limitation of the amount of Ehrlich's claim. The debtors characterize Ehrlich's claim as a claim for damages resulting from the termination of an employment contract thus limiting the amount of the claim under 11 U.S.C. § 502(b)(7).² As authority in support of the request for evidentiary hearing, the debtors cite In re Anthony v. Interform Corp, 96 F.3d 692 (3rd Circuit 1996), for the proposition that the court must take extrinsic evidence to determine the "true substance" of Ehrlich's claim against the debtors. Ehrlich opposes the introduction of extrinsic evidence to determine the true substance of the claim on at least two grounds:

1. The Applicability of Interform.

The Interform case does not stand for the proposition that this court has authority to hear extrinsic evidence to determine the "true substance" of the judgment entered against the debtors. Ehrlich argues that Interform addressed only the issue of whether section 507(b)(7) of the Bankruptcy Code can limit the recovery of a pre-petition judgment creditor in a Chapter 11 bankruptcy proceeding when the creditor's claim arose from the wrongful termination of an employment contract that had been breached over two years before the bankruptcy petition was filed.

The holding in Interform is found at 96 F.3d, 697:

² 11 U.S.C. § 501(b)(7). Allowance of claims or interests. (b) Except as provided in subsections (e)(2), (f), (g), (h) and (i) of this section, if such objection to a claim is made, the court, after notice and a hearing, shall determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount, except to the extent that— . . . (7) if such claim is the claim of an employee for damages resulting from the termination of an employment contract, such claim exceeds . . .

Accordingly, we hold that the express terms of section 507(b)(7) of the Bankruptcy Code mandate that this section be interpreted to place a cap upon *all* employment contract termination claims regardless of whether: (1) the claim has been reduced to judgment; (2) there is any connection between the employee's termination and the debtor's financial problems; and (3) a number of years has passed between the employee's termination and the debtor's filing of the bankruptcy petition.

The sole issue addressed by Interform was whether reducing a breach of employment claim to judgment pre-petition excludes the claim from the limitation of section 502(b)(7). Interform does not address the issue of whether a bankruptcy court should take extrinsic evidence to determine the true substance of the claim of a creditor which is based upon a judgment against the debtor. Therefore, this court holds that Interform does not form a basis for the debtor's request for an evidentiary hearing on the true substance of the claim.

2. Lack of subject matter jurisdiction under the Rooker-Feldman doctrine.

Ehrlich asserts that under the Rooker-Feldman doctrine this court does not have subject matter jurisdiction if the exercise of jurisdiction would result in a reversal or modification of a state court judgment.³ Ehrlich states that to permit extrinsic evidence to determine the true substance of the claim leading to a finding that it is a § 507(b)(7) type claim would put this court in the posture of an appellate court reviewing the findings of fact and rulings of law of the Pennsylvania state court decision. Ehrlich cites Jordahl v. Democratic Party of Virginia, 122 F.3d 192, 202 (4th Cir. 1997), *cert. denied*, 522 U.S. 1077 (1998).

[F]ederal courts are divested of jurisdiction 'where entertaining the federal claim would be the equivalent of an appellate review of the

³ The doctrine was established by two Supreme Court cases (Rooker v. Fidelity Trust Co., 263 U.S. 413, 44 S.Ct. 149, 68 L.Ed. 362 (1923), and District of Columbia Court of Appeals v. Feldman, 460 U.S. 462, 103 S.Ct. 1303, 75 L.Ed 2d 206 (1983). It is predicated on 28 U.S.C. § 1257 which provides that the only federal court to hear appeals from determinations of state courts is the United States Supreme Court.

state court order.’ The controlling question in the Rooker-Feldman analysis is whether a party seeks the federal district court to review a state court decision and thus pass upon the merits of that state court decision, not whether the state court judgment is presently subject to reversal or modification.

The Rooker-Feldman doctrine requires that its applicability be determined before a court considers other defenses.⁴

The court has examined the debtors’ second amended objection to claim. It is clear that the debtors wish to re-characterize the Pennsylvania state court judgment order by introducing evidence. The debtors want to have this court determine that the substantive basis for the Pennsylvania state court’s claim was the breach of an employment contract. Such a ruling would be the equivalent of a decision that the findings of fact by the state court were not supported by the evidence and cannot, therefore, stand as the basis for Ehrlich’s claim.

In response to the debtors’ second amended objection to claim, Ehrlich attached to his memorandum a copy of the Decree Nisi, and the adjudication and final decree of the Pennsylvania state court granting judgment to Ehrlich in the amount of \$611,119.24. This court has examined those decrees and finds no finding of fact to support the argument that the basis for the decision and judgment is grounded in a claim for termination of an employment contract. Rather, the decrees and judgment amount are based upon finding that Ehrlich was oppressed as a minority stockholder in the Audubon Quartet by a majority to his economic detriment⁵, that the debtors are not isolated from liability for their breach of fiduciary duty to Ehrlich, and that the oppressive treatment of Ehrlich by the debtors warrants remedial action by the Pennsylvania

⁴ See, GASH Assoc. v. Village of Rosemont, Ill., 995 F.2d 726, 728-729 (7th Cir. 1993).

⁵ See, page 16 of the Decree Nisi.

state court and that there was found a breach of fiduciary by the debtors.⁶ Finally, the basis for the determination of the amount of the claim for oppression and breach of fiduciary duty was to compensate Ehrlich for his 25% equity share of the Audubon Quartet.⁷ The Decree Nisi of the Pennsylvania state court also disposed of any jurisdictional issues on the theory of waiver.⁸

This court holds that under Rooker-Feldman doctrine it lacks subject matter jurisdiction to receive and consider extrinsic evidence pertaining to the Pennsylvania state court decree.

Having ruled that the Rooker-Feldman doctrine precludes this court's exercise of subject matter jurisdiction, a review of the second amended objection to claim shows that the only remaining ground for objection to the claim is the debtors' assertion that 11 U.S.C. § 502(d)⁹ requires denial of the claim because of a post-petition transaction that is recoverable under 11 U.S.C. § 549.¹⁰ Such a basis for disallowance is, at best, premature. There is no

⁶ *Id.* at pages 17-18.

⁷ *Id.* at pages 19 through 23.

⁸ *Id.* at page 5.

⁹ 11 U.S.C. § 502(d). Notwithstanding subsections (a) and (b) of this section, the court shall disallow any claim of any entity from which property is recoverable under section 542, 543, 550, or 553 of this title or that is a transferee of a transfer avoidable under section 522(f), 522(h), 544, 545, 547, 548, 549, or 724(a) of this title, unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable under section 522(i), 542, 543, 550, or 553 of this title.

¹⁰ 11 U.S.C. § 549. Postpetition transactions. (a) Except as provided in subsection (b) or (c) of this section, the trustee may avoid a transfer of property of the estate—(1) that occurs after the commencement of the case; and (2)(A) that is authorized only under section 303(f) or 542(c) of this title; or (B) that is not authorized under this title or by the court. (b) In an involuntary case, the trustee may not avoid under subsection (a) of this section a transfer made after the commencement of such case but before the order for relief to the extent any value, including services, but not including satisfaction or securing of a debt that arose before the commencement of the case, is given after the commencement of the case in exchange for such transfer, notwithstanding any notice or knowledge of the case that the transferee has. (c) The trustee may not avoid under subsection (a) of this section a transfer of real property to a good faith purchaser without knowledge of the commencement of the case and for present fair equivalent value unless a copy or notice of the petition was filed, where a transfer of such real property may be recorded to perfect such transfer, before such transfer is so perfected that a bona fide purchaser of such property, against whom

adversary proceeding pending which would seek to adjudicate any section 549 matter. In order to prevail on this point, there must be a timely filed complaint, there would have to be an adjudication of recovery under section 549, and a finding of the creditor's failure to pay or turnover.

Conclusion:

Ross W. Krumm

For the reasons stated above, this court will deny the debtors' request for an evidentiary hearing and strike the notice of hearing for June 15, 2005, will deny the second amended objection to claim by the debtors and will allow the claim of Ehrlich as filed.

Accordingly, it is

ORDERED:

That the debtors' request for evidentiary hearing be, and it hereby is **DENIED**, and the matter is stricken from the June 15, 2005 docket; and it is

FURTHER ORDERED:

That the debtors' second amended objection to the Ehrlich claim be, and it hereby is **DENIED** in its entirety, and it is

FURTHER ORDERED:

That the proof of claim filed by David Ehrlich in the above-captioned proceeding be, and it hereby is **ALLOWED**.

Copies of this order are directed to be mailed to Howard J. Beck, Jr., Esquire, P.

applicable law permits such transfer to be perfected, could not acquire an interest that is superior to the interest of such good faith purchaser. A good faith purchaser without knowledge of the commencement of the case and for less than present fair equivalent value has a lien on the property transferred to the extent of any present value given, unless a copy or notice of the petition was so filed before such transfer was so perfected. (d) An action or proceeding under this section may not be commenced after the earlier of—(1) two years after the date of the transfer sought to be avoided; or (2) the time the case is closed or dismissed..

O. Box 21584, Roanoke, Virginia, 24018, counsel for the debtors; to Richard C. Maxwell, Esquire, P. O. Box 14125, Roanoke, Virginia, 24038-4125, counsel for David Ehrlich; and to Margaret K. Garber, Esquire, Office of the U. S. Trustee, First Campbell Square Building, First Street, Suite 505, Roanoke, Virginia, 24011.

Ross W. Krumm
U. S. Bankruptcy Judge